

## WCCF Testimony on Senate Bill 510

Thank you for holding this hearing on SB 510. On behalf of the Wisconsin Council on Children and Families, I'm pleased to testify in support of the bill.

We would like to commend the authors and co-sponsors for crafting a bill that invests in Wisconsin's current and future workforce. Over the long run, that will be the key to the state's economic vitality. Numerous studies have shown that as employers decide where to locate or to expand their operations, the primary factors are considerations like the availability and cost of a high quality workforce, the quantity and quality of public services, proximity to markets, and access to raw materials and supplies.<sup>1</sup> SB 510 recognizes that Wisconsin needs to be competitive in those areas.

As a child advocacy organization, we are particularly pleased that the authors of the bill acknowledge the importance of early education, by seeking to expand the Wisconsin Shares child care subsidy program. That is an expenditure that not only helps our current workforce, by giving more workers access to affordable child care, but it's also an investment in our future workforce. A growing body of research has found that quality early education is one of the most cost-effective investments states can make for long-term economic growth.

Of course, after this bill was initially developed, policymakers received the bad fiscal news that the state is facing a large budget deficit. The deficit and economic downturn underscore the importance of making wise choices about how to invest state resources in ways that ensure long-term economic growth. However, the deficit also limits the options and forces policymakers to consider tradeoffs between the things you would like to do and the sustainability of existing programs.

The state's fiscal problems particularly reinforce one part of SB 510, the provisions that would institute combined reporting of corporate income. Because of the current separate accounting system, corporations now have an incentive to engage in tax avoidance practices. A number of the nation's largest and most profitable corporations have been able to exploit the current system by using gimmicks, such as the so-called Las Vegas loophole, to avoid paying their fair share of Wisconsin taxes.

In light of the state's very large deficit, we no longer have the luxury of looking the other way as these tax avoidance practices proliferate. The largest corporations are getting increasingly sophisticated in devising tax avoidance schemes, and the state's corporate tax code needs to be updated for Wisconsin to be able to afford the programs that keep our state strong and protect the services needed by vulnerable children, families and the elderly.

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<sup>1</sup> See, for example, *Rethinking Growth Strategies: How State and Local Taxes and Services Affect Economic Development*, Robert Lynch, Economic Policy Institute, 2004.

Combined reporting would generate an additional \$90 million per year at a time when the state faces the possibility of deep cuts in critically important state programs. Though it raises revenue, combined reporting does not raise the tax rate or eliminate exemptions, deductions or credits. It makes our tax system fairer, and it should be a part of whatever budget legislation you adopt – whether it's a plan like SB 510 to make investments for long-term economic growth, or a bill to address the large hole in the 2007-09 budget.

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WISCONSIN COUNCIL ON

**children  
& families**

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555 West Washington Ave, Suite 200

Madison, WI 53703

[www.wccf.org](http://www.wccf.org)

☎ 608-284-0580

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## **Combined Reporting Would Close Corporate Tax Loopholes And Preserve Funding for Programs Serving Wisconsin Families**

- **Wisconsin needs to ensure the integrity of its corporate income tax, especially in light of a looming state budget deficit.** In response to preliminary estimates of a \$300-\$400 million shortfall in the budget for the current biennium, many state policy makers have called for spending cuts. These cuts could threaten programs that are essential to the state's most vulnerable children and families.
- **Wisconsin could generate substantial revenue by adopting a tax filing regime known as combined reporting, which would generate about \$90 million a year in tax revenue.** Currently, Wisconsin mandates separate accounting: each corporate entity reports its own income and expenses separately, without regard to the income and expenses of corporations with which it is affiliated.
- **Separate accounting actually encourages corporations to avoid paying Wisconsin tax by shifting income to subsidiaries in other states.** Separate accounting makes it easy for corporations to try to avoid Wisconsin tax through practices like placing investments in Nevada subsidiaries, trademarks in Delaware holding corporations, and land and buildings in real estate investment trusts.
- **These strategies are improper—they have been successfully challenged as lacking business purpose by state tax auditors.** But auditing is a case-by-case approach that succeeds only when firms are audited, auditors are able to identify improper activities and their assessments of additional tax, interest and penalties stand up in court. Often, substantial audit resources are devoted to combating the practices of a few companies, and many improper activities go undiscovered.
- **Combined reporting, which requires a corporation and its subsidiaries to file a combined report of their income and expenses, is a comprehensive, effective solution to corporate tax avoidance.** This filing regime, adopted by 21 of the 45 states with a tax on corporations, eliminates much of the exploitation occurring under separate accounting because it brings back to Wisconsin income that corporations try to shift to other states.
- **Because it raises revenue, critics label it a tax increase—but combined reporting does not raise the tax rate or eliminate exemptions, deductions or credits.** Rather, it ensures that corporations pay tax to the state that they should pay, but may not pay now because of their improper tax avoidance strategies.
- **By combating improper manipulation of corporate structure and accounting practices, combined reporting would make Wisconsin's tax system fairer.** When some businesses are able to skirt their responsibilities for paying for public services, either other taxpayers, both corporations and households, have to pay more or citizens are deprived of the services they need. Combined reporting would also increase the likelihood that corporations will voluntarily comply with the law.



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February 27, 2008

To: Senate Economic Development Committee  
Senator Julie Lassa, Chairman

From: Trisha Pugal  
President, CEO

RE: SB 510 Economic Development Package

On behalf of the over 1,000 lodging properties around the state, we respectfully ask you to amend SB 510 to **remove the Car Rental Tax Increase** as the authorized source of funding for the KRM Commuter Rail project.

While the KRM Commuter Rail Project may be of great value to commuters in southeastern Wisconsin, a dramatic increase in a tax on travelers renting cars who by definition will not be using the commuter rail transportation, is excessive and a detriment to attracting travelers to our state.

Some may say that the language authorizes the Regional Transit Authority (RTA) to submit a referendum to the voters in the district asking if they support such a tax on car rentals, making the RTA appear to be honoring the will of the voters, this referendum is not required (only authorized if the RTA wishes) and is only advisory. First of all, giving voters the opportunity to impose a tax on out-of-town individuals to pay for a service used by the voters, so it will not cost the voters, will generate a predictable approval. And for some reason if not, the RTA is not bound by the results of the referendum and can impose the tax increase anyway.

This tax increase from \$2 to \$15 on top of the many taxes already on car rentals, will make southeastern Wisconsin a very high taxed car rental region for those flying into Milwaukee's Mitchell Field, with plans to travel to not only southeastern Wisconsin, but also to other areas of the state. Wisconsin works hard to market our state as a great place to visit, and relies heavily on the state sales tax revenue generated by travelers to our state. Let's not create a barrier to send them to other states instead.

Please remove the Car Rental Tax Increase authorization from SB 510.

**TO:** Senate Committee on Tax Fairness and Family Prosperity

**FROM:** Community Bankers of Wisconsin      Metropolitan Milwaukee Association of Commerce      Midwest Food Processors Association

Wisconsin Bankers Association      Wisconsin Economic Development Association      Wisconsin Engine Manufacturers and Distributors Alliance

Wisconsin Manufacturers & Commerce      Wisconsin Merchants Federation      Wisconsin Mortgage Bankers Association

Wisconsin Motor Carriers Association      Wisconsin Paper Council      Wisconsin Petroleum Council

Wisconsin Restaurant Association      Wisconsin Utilities Association      Wisconsin Utility Investors, Inc.

**RE:** Coalition Against Combined Reporting  
**DATE:** February 14, 2008  
**CC:** Wisconsin Senate  
Wisconsin Assembly

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The Senate Committee on Tax Fairness and Family Prosperity has recently held informational hearings on the issue of combined reporting for corporate income taxation with national speakers who favor this method of increasing corporate income taxes. In addition, Senate Democratic leadership has proposed combined reporting as a component of its "economic development" package.

The Wisconsin business community is united in its opposition to combined reporting. This proposal is a job-killer that will make Wisconsin a significantly less competitive place to do business. The above organizations strongly discourage this Committee and the Senate as a whole from advancing such a proposal.

### **COMBINED REPORTING**

Wisconsin law currently uses separate entity reporting and imposes corporate franchise or income taxes on each separate corporation doing business in Wisconsin. These separate entities file separate tax returns reporting net income. Combined tax reporting requires that two or more related entities engaged in businesses inside *and* outside of Wisconsin calculate their tax burden as a single unit under the apportionment formula. This is a radical change in the way corporate income taxes are calculated and could impose Wisconsin taxes on economic activity outside of Wisconsin. It is a significant disincentive to do business in the state and will inevitably lead to taxing income earned from entities without nexus in

Wisconsin. The non-partisan Legislative Fiscal Bureau estimated that passing combined reporting represents a **\$90 million tax increase for Wisconsin businesses, or greater than 10 percent increase in corporate income tax collections.**

In addition to increased taxes, combined reporting imposes significant administrative burdens on taxpayers who are already dealing with an overly complicated state tax code. For example, the definition of "unitary business" is a subjective determination, giving the Wisconsin Department of Revenue significant arbitrary authority to impose taxes on Wisconsin companies. Even where critical factors are well defined, disagreements in other states over what should be included in a combined return have often needed to be decided by costly litigation. These complexities are particularly burdensome for small to medium sized multi-state companies.

The complexity of combined reporting also arbitrarily distorts the income of employers. Such a distortion negatively affects job growth by creating uncertainty and, therefore a disincentive for investment.

Finally, combined reporting is a new, different corporate income tax system, not merely a "loophole closer". The Wisconsin Department of Revenue presently has the authority, under the sham transactions statute, to audit and assess taxes on transactions it believes solely exist for the purpose of tax avoidance.

### **WISCONSIN TAX CLIMATE**

The national, non-partisan Tax Foundation ranks Wisconsin's business tax climate as only the 39<sup>th</sup> best, or 12<sup>th</sup> worst, in the nation. Forbes magazine recently ranked Wisconsin as the 44<sup>th</sup> best state, or 7<sup>th</sup> worst, in which to do business. A corporate tax increase of more than 10 percent can only reduce Wisconsin's standing on these competitive indices. That is the wrong direction, particularly as the state's economy teeters on the edge of recession.

While some argue that Wisconsin's corporate income tax rates are not amongst the highest in the nation, many states in the region have lower rates, and nationally four states have no corporate income tax at all. Multi-state corporations already pay their fair share of taxes in Wisconsin. According to the Department of Revenue, multi-state corporations account for only 35 percent of the filing corporations, yet paid 71 percent of the total tax liability.

In addition to corporate income taxes, corporations in Wisconsin pay real property taxes, personal property taxes, sales taxes, payroll taxes, UC taxes, recycling taxes and environmental fees; and in some cases, gross receipts taxes. Corporate profits are also often subject to double taxation; once as corporate income, and again as personal income when paid out as dividends to individual shareholders.

In a state with such a high tax burden, public debate should be focused on tax cuts, not tax increases. Again, we strongly encourage Wisconsin Legislators to reject any proposal on combined reporting, and focus efforts on improving Wisconsin's business climate rather than creating additional costs that make us less competitive.

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PO Box 473  
Milwaukee, WI 53201

414-231-5000

Senator Russ Decker

February 26, 2008

Dear Senator Decker:

Please register me as a strong supporter of the KRM commuter rail project in southeastern Wisconsin. As a vital link in our state's transportation network, the Milwaukee to Chicago corridor provides particularly vibrant opportunities for Wisconsin's economic growth and global competitiveness. In addition, easily accessible regional transportation options are critical to attracting and retaining a talented and qualified workforce who are increasingly mobile and who expect convenient, affordable public transit as an employment benefit.

As a business leader in our community, our state, and, now, in the Chicago area, I have seen and experienced firsthand how critical this rail corridor is for our region's economic health and, indeed, its survival. Making commuter rail a reality would not only bring major development to the area and create new jobs, it would increase property values (and, thus, local revenues and property tax relief), grow General Mitchell International Airport, enhance Wisconsin's tourism industry, expand access to educational institutions, and diversify our human resource potential. Moreover, without regional public transportation, I very much fear that our state's economic health will be in jeopardy. Nearly all other major urban areas of our size now provide these regional transit choices, and, frankly, we simply cannot afford to be without them if want to retain our future economic viability.

Senator Decker, I do truly appreciate all the Senate Democrats have done thus far to ensure KRM becomes a reality. Now, though, I urge you and your colleagues to redouble your efforts to secure this much-needed rail link for our region and state.

Sincerely,

*Bob Mariano*

Robert A. Mariano  
Chairman & CEO



**Testimony on SB510 (Combined Reporting Corporate Income)**  
**For the Wisconsin Senate Committee on Economic Development**  
Feb. 27, 2008

**Jack Norman**  
**Institute for Wisconsin's Future**

I am speaking in support of that part of Senate Bill 510 which would implement combined reporting for the Wisconsin corporate income tax.

The Institute for Wisconsin's Future has done considerable research on Wisconsin's tax system, especially the state corporate income tax. We are a philanthropy-funded research and public education non-profit based in Milwaukee. I am IWF's Research Director (email: [jnorman@wisconsinsfuture.org](mailto:jnorman@wisconsinsfuture.org); web: [www.wisconsinsfuture.org](http://www.wisconsinsfuture.org))

Wisconsin's corporate income tax—along with many other parts of Wisconsin's tax code—has become out-of-date. While corporate tax practice has evolved rapidly, especially since the turn of the century, Wisconsin's corporate tax structures have failed to keep pace. The absence of combined reporting is one major symptom of this failure to bring our tax system into the 21<sup>st</sup> century.

Combined reporting would modernize the state's corporate income tax system by requiring all corporate filers to combine results for all firms in their corporate family. Under the current system, corporations with operations in multiple states (and countries) are able to engage in internal transfers of funds from Wisconsin to other states in ways that allow them to avoid Wisconsin taxes altogether. Such tax-avoidance techniques were hardly used when our corporate tax system was created, at a time when far fewer companies had subsidiaries in so many different tax jurisdictions. But corporate tax structures have changed considerably since the early days of the corporate income tax, while the tax itself has been relatively unchanged.

Already by 1997, major flaws in the corporate income tax were depriving the state of million of dollars of revenue. A case in point is Wal-Mart. The Wisconsin Department of Revenue concluded that from February 1997 through January 2000, Wal-Mart improperly avoided paying income tax on over \$104 million in profits. The state is seeking payment of the missing \$8.3 million in income tax, plus interest and penalties. Wal-Mart has challenged, and the case is currently before the state Tax Appeals Commission. At issue is Wal-Mart's use of a real estate investment trust through which the firm in effect paid rent to itself in a manner allowing it to shelter significant profits.

Had combined reporting been in effect, Wal-Mart would have paid the full tax years ago and there would be no expensive, time-consuming, disruptive litigation. Nor would there have been the risk that Wal-Mart's position is upheld by the Tax Appeals Commission, thereby endorsing the technique for an unknown number of other corporations.



The problem continues. Data from IWF from the Department of Revenue show that in 2005 over 60% of large corporations that filed income tax returns claimed no tax liability. Such highly profitable, multinational firms as Microsoft and Merck are among the many companies that did considerable business in the state, acknowledged an obligation to file a state tax return, but claimed zero taxable profits from Wisconsin. Neither Microsoft nor Merck, among many others, paid a penny in Wisconsin income tax.

By 2006, corporate tax avoidance in Wisconsin had grown to the point where there was an estimated \$643 million in corporate tax leakage. This leakage is the loss of state revenue due to tax avoidance using tax breaks, credits, loopholes and other profit shelters. (For details, see IWF's report, *Wisconsin's Revenue Gap: An analysis of corporate tax avoidance*.) Even after allowing that on the order of \$100 million of this may have been targeted for economic development efforts, that still leaves over five hundred million dollars in tax avoidance because of tax law loopholes.

But it would be wrong to say that this situation is simply the result of 'Bad Corporate Behavior' such as 'Bad Wal-Mart' or 'Bad Microsoft.' It is Bad Tax Laws that make corporate tax avoidance possible. The laws are inadequate to stop the behavior. Wisconsin's unwillingness to modernize its corporate income tax has cost the state hundreds and hundreds of millions of dollars in uncollected revenue.

Combined reporting is hardly a novel and untried technique for modernizing state corporate income tax. It was first implemented in 1937 by California. Since then, twenty-one other states have followed, including five in just the past three years.

Does combined reporting hinder economic growth? No. The evidence is clear. As *Governing* magazine reported in its January 2008 review of 'Growth & Taxes:' "There is no evidence that the economies of combined-reporting states have suffered compared with those without combined reporting."

Michael Mazerov, a national expert on state tax policies, last month told the Wisconsin Senate's Committee on Tax Fairness and Family Prosperity that his research showed that nine of the ten states with the fastest growth in manufacturing employment were combined reporting states. Mazerov also noted that a U.S. Small Business Administration study found greater entrepreneurship in combined reporting states.

"Aggressive tax avoidance by large, sophisticated multistate companies is a serious and growing problem," Mazerov told the committee. "Unfortunately, Wisconsin remains something of a laggard among the states in seeking to address it," he continued. "The primary problem is that the state's corporate tax code has not been updated to reduce the opportunities for tax avoidance that are now open."

There's much that needs modernizing in Wisconsin's tax code. But especially with the weak economy undermining state revenue estimates, the enactment of combined reporting is an extremely timely modernization that would prevent serious revenue erosion. We urge the committee to approve SB510.



## STATE SENATOR PAT KREITLOW

**Sen. Pat Kreitlow remarks  
Senate Dems Economic Development Package  
February 27, 2008**

Governor Doyle's State of the State address recognized the challenges and the opportunities of the Wisconsin economy, and after the speech I said many of my colleagues would also propose ideas for moving Wisconsin forward.

Increased tax credits for companies that add jobs through research and development can be a very valuable tool, and I'm happy to be one of the co-authors of what Governor Doyle wants to accomplish. But we also need to take some bold steps for immediate job creation in other ways, and today's package of proposals in Senate Bill 510 does just that.

Let me briefly describe the main elements of the bill.

Wisconsin needs to invest directly in infrastructure. Years of neglect in the roads and bridges that keep our economy strong are starting to show. We can address that with a \$50 million increase for road rehabilitation and highway development. That translates into 2,500 good paying jobs in our state.

Wisconsin needs to invest directly in jobs. We have waiting lists at our technical colleges in some of the areas where skilled labor shortages are holding back the Wisconsin economy. We can address that with increased funds for skills training, financial aid and child care assistance for working families.

Next, we're going to beef up a program with a proven record of success in key parts of the state: the Technology Zone tax credit program that helps businesses fund the creation of new jobs in rapidly growing fields like advanced manufacturing. This bill adds more tax credit opportunities to technology zones without placing any new burden on state coffers. Instead, we would reallocate some credits from other programs that are getting little or no use.

The I-94 Technology Zone in western Wisconsin, for example, has leveraged fewer than \$5 million in credits to help create more than 600 jobs. The zones in northeast Wisconsin and around Madison are also in need of making sure this successful program can continue.

This committee is on record in support of efforts to reconfigure all of our state's tax credit programs to make them easier to track and easier to use so that unallocated

credits can be put to good use elsewhere instead of wasted. But should that effort fall short in this session and our current zones are still in effect, we need to beef up the zones that are working right now.

The next area I'll address in the bill is an additional \$8 million in grants and loans to businesses involved in the research and development of renewable energy. This is funding that was cut during the budget process but is greatly needed to secure Wisconsin's leadership in developing energy from renewable sources. Our neighboring states are all ready to take those jobs—in research, in production, in farming and in distribution—if we drop the ball.

This is about energy security for our country. It's about jobs throughout rural Wisconsin. It's about cleaner burning fuels for the southeastern part of the state. It's about the timber and paper industries that can find new uses for their by-products. And it's about time we truly invested in all the jobs that renewable energies can create.

SB 510 makes a further investment in economic development in the southeast part of the state by giving state approval for the KRM rail line, a vital link for job growth from Milwaukee to Chicago.

That's what SB 510 does. Now let's focus on how to pay for it. And as a member of the Committee on Tax Fairness and Family Prosperity, I'm proud to show how members of this legislature are working to undo years of abuse and inattentiveness that have plunged our state's tax infrastructure into disarray at the expense of families. We need to get our fiscal house in order. Many have chosen to ignore half of the equation and focus on ways to slash vital services. Senate Bill 510 takes off the blinders and helps shine a light on tax loopholes that have grown large enough to drive a Brinks truck through.

Closing those loopholes is not partisanship. It's sound economic policy. It's pro-business for those businesses who play by the rules, who invest in people and infrastructure without using high-paid lawyers and accountants to shirk their share of helping pay for all that they use. Wisconsin companies use Wisconsin infrastructure and well-educated Wisconsin people. Whenever a corporation cheats taxpayers out of dollar, that's a dollar that comes from middle class families already playing by the rules. It's time to end that imbalance. In return, we can both pay for economic development packages and reduce corporate tax rates in the future.

And in return, it's high-time we invested in the businesses that play fair, take risks, and create the jobs that grow Wisconsin. SB 150 does that, and I urge your support for this endeavor.